STATE OF COLORADO

OFFICE OF THE GOVERNOR

136 State Capitol
Denver, CO 80203 - 1792
Phone (303) 866-2471

John W. Hickenlooper
Governor

April 16, 2015

The Honorable Dickey Lee Hullinghorst
Speaker, House of Representatives

The Honorable Bill Cadman
President, State Senate

The Honorable Brian DelGrosso
Minority Leader, House of Representatives

The Honorable Morgan Carroll
Minority Leader, State Senate

Colorado General Assembly
State Capitol Building
200 E. Colfax
Denver, CO 80203

Dear Colleagues,

As the 2015 legislative session enters its final weeks, I extend my congratulations to you for your leadership on many important decisions and thoughtful debate about the needs of our state. Of particular note is the exemplary and intensive bipartisan work to craft a budget that strikes the appropriate balance between many competing and worthy priorities.

There is other work required to prudently position our state's financial resources, not just for next year but for many years down the road. In the wake of the Great Recession, we can see that support for working and middle class families, and restoring cuts to transportation and education are critical remaining items that the FY 2015-16 budget cannot address by itself. In the remaining time we have left in this legislative session, I am asking for your partnership to take several bold steps with these priorities in mind.

Recent revenue forecasts from the Office of State Planning and Budgeting and the Colorado Legislative Council Staff illustrate both the economic growth in our state but also the complex and contradictory nature of multiple laws and constitutional rules. They call for limits on revenue and increases in spending, as well as new ongoing tax credits. However, the five-point plan we are outlining here finds a balance in these contradictions and makes it possible to build and maintain our roads and bridges and restore some cuts to education while providing rebates and a bit of relief to Colorado's middle class.

When we look beyond FY 2015-16, two statutes from 2009 are significantly affecting the resources in the General Fund: House Bill 09-1293, which created the hospital provider fee and Senate Bill 09-228, which created automatic increases in transportation and capital construction funding from the General Fund if certain economic triggers are met.

Endorsed by many hospitals in 2009, the Hospital Provider Fee is a charge on patient revenue remitted by hospitals to the state so that we can receive matching federal funds. To a large extent, these funds pay for expanded Medicaid populations for which previously hospitals were receiving insufficient compensation. Under the current program design, the hospital provider fee counts toward the State's revenue cap under the Taxpayer's Bill of Rights (TABOR). In the current year, we expect provider fee collections to reach $532.3 million, and in FY 2015-16, they will grow to $688.5 million. When combined with the economic recovery, this additional revenue, which was not collected by the State when the revenue cap was set in FY 2007-08, is a significant contributing factor to the excess revenues we see in both forecasts.

Looking back at the program design, we can see that the hospital provider fee could have been implemented differently. Though the hospital provider fee is <u>not</u> collected in the General Fund it counts toward the revenue limit. These funds are earmarked for health care and <u>cannot</u> go to pay rebates. If, instead, the hospital provider fee were designated as an enterprise fund, these funds would not apply to the revenue limit and thus not contribute to rebates. Without a change, rebates that result because of the hospital provider fee will be paid at the expense of our roads, schools, and other items supported by the General Fund.

Senate Bill 09-228 established a formula that would, as the economy recovered, direct specific amounts of General Fund revenue to capital construction and transportation. However, when there is a TABOR rebate, the transfers are reduced or eliminated. The size of the projected TABOR rebates are inflated by the hospital provider fee such that the transfers to high priority transportation projects will be reduced to <u>half</u> the potential amount in FY 2015-16 ($205.2 million to $102.6 million), and depending on the forecast, eliminated in future years.

In the current year and in FY 2015-16, the range of projected rebates that will be returned to taxpayers under formulas that have evolved over many years includes a sales tax rebate and possibly an enhancement of the federal Earned Income Tax Credit (EITC). If the EITC rebate is triggered, it will become a permanent tax credit in subsequent years, paid from the General Fund.

As we have evaluated these interactions and researched the legislative history of these laws, it has become clear that we can do better as a state to provide for key priorities such as transportation, education, and supporting the middle class, while still respecting the will of the voters to limit state government revenue.

After hearing from many stakeholders and much consideration, we ask the General Assembly to consider the following legislative initiatives.

First, we propose that the entire TABOR surplus be rebated in FY 2014-15 and FY 2015-16. There is a range of possible ways that rebates could be paid out, either through the sales tax rebate or through the EITC, or both. Most of these formulas were adopted many years ago and, in the aftermath of two recessions since that time, we believe the rebate structure needs to be updated.

We agree all Colorado families should receive rebates, but we propose that the TABOR rebates focus on working and middle class families. There is wide research that shows the benefits of the EITC for low- and moderate-income working families. We should agree on a change to the current system of rebates that would direct a larger share of the sales tax rebate to middle income families.

Second, beginning in FY 2016-17, the hospital provider fee should be converted to a fee that is collected in an enterprise fund. Because the fees were endorsed by the payers and because they are discretely earmarked for health care only, enterprise designation is both logical and appropriate. Also, prior to the implementation of the hospital provider fee, the non-partisan Office of Legislative Legal Services determined that the new fee could not be deemed a tax. Thus, we see no compelling reason why this program should cause any "crowding out" of legitimate and worthy state priorities like transportation and education in the General Fund. By moving the funds to enterprise status, revenue classified under TABOR will drop substantially. Rebates, however, would continue under the EITC in an annual amount of approximately $85 million and perhaps under the reformed sales tax rebate.

Make no mistake: we are not proposing any expansion of the hospital provider fee or the Medicaid program.

Third, relative to current law, the second change above allows the full transfer to transportation to occur - estimated at approximately $215 million in FY 2016-17. General Fund support for transportation has a long history in Colorado, but no transfers have occurred since FY 2007-08. Though Colorado has been blessed with robust growth for the past few years, the declining purchasing power of the fuel tax and the impact of the recession have both affected our transportation system. The financing system has struggled to keep pace with the increase in passenger and freight vehicle traffic.

By securing the return of funding for transportation we can start building a mix of new high-priority transit and highway projects. Working with local partners across the state, the Colorado Transportation Commission has identified a list of 50 important projects at a total cost of $2.3 billion that will ease congestion and prepare Colorado for the influx of people and goods we know are coming in the future. This investment will benefit Colorado for years to come and will spur economic growth in key transportation corridors - both rural and urban - and in adjacent communities.

Fourth, this change also creates a new ability for the state to dedicate new resources to buying down the negative factor in K-12 school finance. Based on current projections, we should dedicate $50 million above enrollment and inflation costs in FY 2016-17 and apply this amount to reducing the negative factor. Although less than ten percent of the negative factor now, this additional contribution to K-12 support reflects continued progress that began in FY 2014-15 and is expected in FY 2015-16.

Fifth, we should agree on a mechanism that repays the severance taxes used to balance the current budget as well as the $75 million of hospital provider fee money that was transferred to the General Fund during the Great Recession.

Colorado has great needs and extraordinary budgetary constraints. The five-point plan outlined above provides some measure of simplification of the rules we have and strikes a balance between limiting our revenue and addressing the needs of a growing state.

I look forward to hearing from you and working together on a solution that serves all of Colorado.

Sincerely,

John Hickenlooper
Governor

Cc: Colorado General Assembly